

JEFF FLAKE
ARIZONA

SR-413 RUSSELL SENATE OFFICE BUILDING
(202) 224-4521
COMMITTEE ON FOREIGN RELATIONS
COMMITTEE ON
ENERGY AND NATURAL RESOURCES
COMMITTEE ON THE JUDICIARY
COMMITTEE ON AGING

United States Senate

WASHINGTON, DC 20510-0305

August 19, 2016

STATE OFFICES:
2200 EAST CAMELBACK ROAD
SUITE 120
PHOENIX, AZ 85016
(602) 840-1891

6840 NORTH ORACLE ROAD
SUITE 150
TUCSON, AZ 85704
(520) 575-8633

The Honorable Richard Cordray
Director
Consumer Financial Protection Bureau
1700 G Street, NW
Washington, DC 20552

Dear Director Cordray:

I am concerned about the Consumer Financial Protection Bureau Notice of Proposed Rulemaking on pre-dispute arbitration related to consumer financial products. The prerequisite study your agency conducted does not adequately support the criteria in the proposal as federal law requires.

Since Congress passed the Federal Arbitration Act in 1925, federal law has protected the use of arbitration as a means to resolve private disputes. As an alternative to expensive litigation, millions of Americans have since enjoyed the faster resolution time associated with arbitration. Arbitration is also less costly than litigation for consumers because most arbitrators are limited in the fees they can charge for their services. The use of class-action waivers, which the Supreme Court ratified as recently as 2011, allows financial institutions and consumers to resolve their disputes in arbitration rather than entering into costly class litigation. Eliminating the availability of these waivers, as the Bureau proposes to do, would put financial institutions and their customers at the mercy of those looking to initiate lengthy court proceedings that yield little benefit to either the consumers or the institutions.

As you know, Section 1028 of the Dodd-Frank law required the Bureau to conduct a study on arbitration and authorized the Bureau to issue a regulation to “prohibit or impose limitations” on arbitration agreements. However, under current statute, such regulations are permissible only if the study finds that they are “in the public interest and for the protection of consumers.” Upon reviewing the study, I have concerns about the extent to which it justifies the Notice of Proposed Rulemaking. First and foremost, the benefit of class settlements to consumers is very much an open question, yet the Bureau appears to have chosen a side while failing to fully consider the ramifications and effect on protections afforded consumers. For example, the study did not investigate whether class counsel act in good faith as agents of class litigants.

Given the potential impacts and the explicit statutory threshold required for agency action, I request your answers to the following questions. Please provide any and all documentation that supports your answers.

1. The study compares total awards from class action settlements over a five-year period with arbitral awards over only a two-year period.

- a) Please explain why, given the inherent differences between settlements and damage awards, the Bureau believes this to be an apple-to-apple comparison?
 - b) Please explain why, given the inherent differences between settlements and damage awards, the Bureau did not compare class action settlements to pre-arbitral alternatives like mediation and “customer service” settlements?
2. On what basis did the Bureau exclude data on arbitral settlements? On what basis did it exclude data on mediation and “customer service” settlements?
3. Please describe any and all of the alternatives to the proposed new regulatory regime that the Bureau considered.
4. Is it possible for arbitration agreement between consumers and financial institutions to be fair and non-deceptive? If yes, would such an agreement meet the Bureau’s approval?
5. The Bureau has only operated since July 2011. In that time, it has supposedly recovered \$11.2 billion for consumers through enforcement actions and \$300 million through supervisory actions.
 - a) Given the Bureau’s enforcement record since July 2011, why did the Bureau deem it appropriate to only study data from 2008 to 2012?
 - b) What effect does the existence of the Bureau’s enforcement power since July 2011 have on the net benefit of class actions?
6. The Arbitration Rule is based on the premise that banning the use of agreements that prohibit class-action lawsuits is “in the best interest of the public.” However, in many instances, attorney fees comprise large portions of the aggregate payments made to classes in settlements. As Judge Richard Posner has observed:

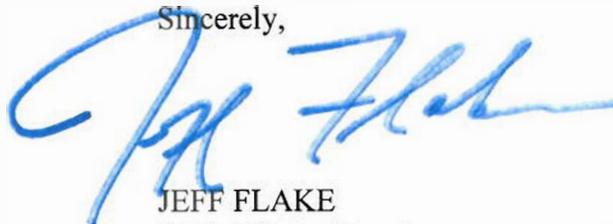
[C]lass counsel ... have an opportunity to maximize their attorneys’ fees ... at the expense of the class. The defendant cares only about the size of the settlement, not how it is divided between attorneys’ fees and compensation for the class. From the selfish standpoint of class counsel and the defendant, therefore, the optimal settlement is one modest in overall amount but heavily tilted toward attorneys’ fees. *Eubank, et al. v. Pella Corp. & Pella Windows & Doors, Inc.*, 753 F.3d 718, 720 (2014).

Indeed, the Bureau's study confirmed this, finding that in settlements of \$100,000 or less attorney fees comprised 57 percent of total payouts.

- a) Did the Bureau consider placing a limit on the percentage of fees an attorney can demand in a lawsuit?
 - b) What would you consider to be a reasonable range of attorney fees by percentage of payments made in a settlement? Why?
7. You stated on February 16, 2016, "the Bureau's rule requires companies to provide the Bureau with arbitral claims and awards, which might be made public, the proposals we are considering would bring the arbitration of individual disputes into the sunlight of public scrutiny." You have argued that this information is vital in evaluating arbitration. If the information is vital to evaluate the effectiveness of arbitration, why didn't the Bureau require it in the study?
 8. Did the Bureau consider whether the restriction of mandatory arbitration agreements would affect the availability of arbitration as a means to settle disputes between consumers and financial institutions? If so, why did the Bureau disregard this concern?

Thank you for your attention to this matter, in strict accordance with existing rules, regulations, and ethical guidelines. Should you have any questions, please contact Nick Morrison in my office at [REDACTED]

Sincerely,



JEFF FLAKE
United States Senator